

Members:

Sen. Tom Weatherwax, Chairperson
Sen. Richard Young
Sen. James Merritt
Sen. Katie Wolf
Rep. Markt Lytle
Rep. Claire Leuck
Rep. James Buck
Rep. William Friend

Advisory Members:

Herschel Cook
David Butterfield
Barbara Haas
Karen Large
Howard Hatcher
William Goffinet
James Murphy
Judith Anderson
Eugene Hostettler
Stephen Queior
David Bennett
Michael Claytor

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Authority: P.L.242-1997



LOCAL GOVERNMENT FINANCE STUDY COMMISSION

Legislative Services Agency
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MEETING MINUTES

Meeting Date: October 28, 1998
Meeting Time: 10:00 A.M.
Meeting Place: State House, 200 W. Washington St.,
Room 431
Meeting City: Indianapolis, Indiana
Meeting Number: 4

Members Present: Sen. Thomas Weatherwax, Chairperson; Sen. Richard Young; Rep. James Buck; Rep. William Friend; Herschel Cook; Karen Large; Judith Anderson; James Murphy.

Members Absent: Sen. James Merritt; Sen. Katie Wolf; Rep. Markt Lytle; Rep. Claire Leuck; David Butterfield; Barbara Haas; Howard Hatcher; William Goffinet; Eugene Hostettler; Stephen Queior; David Bennett; Michael Claytor.

1. Call to Order

Senator Tom Weatherwax, the Chairman of the Commission, called the meeting to order shortly after 10:00 a.m.

2. Discussion Concerning School Property Taxes

Senator Weatherwax began the meeting by stating that he hoped to address two issues: (1) the elimination of school general fund and transportation fund property taxes; and (2) how to respond to any shifting of the property tax burden onto homeowners if the Indiana Supreme Court decides the *Town of St. John* case by requiring some form of market value assessment.

Senator Weatherwax noted that the most recent studies had estimated that market value assessments would lead to an approximately 31% increase in the property tax burden of homeowners. He explained that this would represent an increase of almost \$569 million in property taxes, which is roughly equivalent to the school general fund and school transportation fund property taxes that will be paid by homeowners in 2000. Senator Weatherwax stated that the elimination of school general fund and transportation fund property taxes would therefore hold homeowners harmless from any burden-shifting resulting from market value assessments.

He then discussed how the approximately \$1.5 billion in revenue lost from the elimination of school general fund and transportation fund property taxes could be replaced. For purposes of discussion by the Commission, Senator Weatherwax described a proposal that would replace the lost property tax revenue by increasing various state taxes. Under this proposal: (1) the individual adjusted gross income tax rate would be increased from 3.4% to 3.9%; (2) the corporate adjusted gross income tax rate would be increased from 3.4% to 4.2%; (3) the supplemental net income tax rate would be increased from 4.5% to 5.3%; (4) the financial institutions tax rate would be increased from 8.5% to 8.6%; (5) the sales tax rate would be increased from 5.0% to 5.5%; and (6) the sales tax would be extended to services other than medical and legal services.

Senator Weatherwax then called on Diane Powers and Bob Sigalow of the Legislative Services Agency's Office of Fiscal and Management Analysis to discuss a memorandum they had prepared describing the potential property tax savings from the elimination of school general fund and transportation fund property tax levies and also specifying how much replacement revenue would be generated by the proposed increases in state tax rates.¹

After a discussion of the memorandum by Commission members, Senator Richard Young stated that he was concerned with replacing school general fund and transportation fund property taxes with increased state taxes, because the state taxes are more sensitive to changes in the economy. He questioned what would be done during a recession to ensure that education funding did not suffer. Representative Jim Buck commented that he believed Senator Young's concerns were valid, but suggested that a state "rainy day fund" for education funding could be established. Senator Weatherwax noted that such a fund had not been included in the proposal before the Commission.

Representative Buck stated that a fundamental issue is whether the replacement

¹Copies of the memorandum prepared by LSA's Office of Fiscal and Management Analysis are on file in the Legislative Information Center, Room 230, State House, Indianapolis, Indiana 46204. The telephone number of the Legislative Information Center is (317) 232-9856, and the mailing address is 200 W. Washington St., Suite 301, Indianapolis, Indiana 46204-2789.

revenue should be raised through local taxes or through state taxes, and he said that he believed control over the level of taxation for education should be a local decision. He suggested that a local income tax for education might be the best way to replace revenue lost from the elimination of school general fund and transportation property taxes. Senator Young noted that local income taxes for education had been proposed in the past. He stated that some school districts could generate the necessary revenue, but in poorer counties it would take a high local income tax rate to generate that revenue. Representative Buck stated that this problem could be addressed by changing the state school funding formula to provide that the state would pay for shortfalls in school districts that could not raise sufficient revenue.

Representative William Friend asked staff several questions concerning the proposal to expand the sales tax to include services. He also asked how much revenue would be generated by raising the sales tax rate from 5.0% to 5.5%, but not expanding the sales tax base to include services. The Commission's fiscal analysts stated that such an increase in the rate would most likely raise between \$400 million and \$450 million.

Representative Buck noted that the proposal being discussed by the Commission was on its face revenue neutral, but that it did not factor in additional tax revenue that would be generated by the increase in economic activity that would result from the elimination of school general fund and transportation fund property taxes, especially the elimination of the school property taxes that had been imposed on business inventory. Mayor Herschel Cook stated that he would be in favor of eliminating property taxes on inventory as quickly as possible. He agreed with Representative Buck that increased economic activity would result from the elimination of inventory taxes, and that this increased activity would lead to greater state tax revenue even without an increase in state tax rates. Mayor Cook also stated that he would rather see property tax replacement revenue raised from a higher sales tax rate than an expansion of the sales tax to include services.

Ms. Karen Large commented that as a county auditor she has experienced problems with the distributions of the existing local income taxes, and that she was worried that similar problems would occur with the distribution of a local income tax for education. Ms. Large also questioned what revenue would be used to replace lost property tax revenue that had been dedicated to paying bonds issued in tax increment financing districts.

Representative Buck stated that the General Assembly should also consider enacting limits on the growth of state and local spending. He stated that with these limitations, school property taxes could be replaced with a much lower increase in income taxes.

3. Taxation of Railroad Car Companies

Senator Weatherwax then discussed Preliminary Draft 3620, concerning the taxation of

railroad car companies. He explained that the draft would do the following:

- (A) Provide that the property taxes derived from indefinite-situs distributable property of railroad car companies are deposited in the State General Fund, instead of the Commuter Rail Service Fund.
- (B) Grant railroad car companies a credit against their indefinite-situs property tax liability for railroad car maintenance and improvement expenditures made in Indiana. This credit would be equal to 50% of the qualified expenditures made by the taxpayer in the taxable year.
- (C) Provide that 0.17% of state sales tax revenue is distributed to the Commuter Rail Service Fund. This would be roughly equal to what the NICTD currently receives from property taxes deposited into the Commuter Rail Service Fund.²

Senator Weatherwax stated that the draft would remove the indefinite-situs property tax as a source of NICTD funding, and it would also provide an incentive for railroad car companies to expand their business in Indiana, thereby creating more jobs. Senator Weatherwax stated that he believed that the credit would lead to greater railroad car maintenance and repair activity and higher employment, which would in turn generate tax revenue that would at least partially pay for the cost of the credit.

Senator Weatherwax recognized Mr. Rex Richards of the East Chicago Chamber of Commerce. Mr. Richards stated that he supported the proposal and that he believed the property tax credit would prove to be a useful economic development tool. Senator Weatherwax then recognized Mr. Louis Mazucca, the State Tax Manager for the General Electric Rail Car Company. Mr. Mazucca stated that he supported the proposal, and he commented that the current tax structure provides a disincentive that deters railroad car companies from bringing railroad cars into Indiana for repair.

Mr. Kent McDaniel of the Indiana Transportation Association, representing the Northern Indiana Commuter Transportation District (NICTD), stated that NICTD also supported the proposal.

4. Next Meeting Date; Adjournment

After thanking the Commission members and witnesses for their attendance at the meeting, Senator Weatherwax stated that the Commission's next meeting would be held on November 18, 1998, at 10:00 a.m. in the State House. Senator Weatherwax then adjourned the Commission meeting.

²Copies of PD 3620 are on file in the Legislative Information Center. See footnote 1.